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C O N F I D E N T I A L SECTION 01 OF 02 BUENOS AIRES 001396

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TAGS: EFIN ECON ETRD PREL AR
SUBJECT: GLOBAL ECONOMIC CRISIS COMPLICATES ARGENTINA'S
RE-OPENING OF THE DEBT EXCHANGE FOR HOLDOUTS

REF: A. BUENOS AIRES 1330
¶B. BUENOS AIRES 1312

Classified By: Ambassador E.A. Wayne for Reasons 1.4 (b,d)

Summary

¶1. (C) The global financial crisis is complicating negotiations between private foreign banks and the GoA over the reopening of both the debt exchange to Holdout bondholders and the simultaneous debt swap for bonds coming due 2009-2011. GoA and Citibank contacts confirm that no deals are possible in the current market, given that yields on Argentine sovereign bonds have spiked over 20% in recent weeks. Nevertheless, the two sides hope to complete negotiations over the next few months to have the two transactions ready to launch as soon as there is a market window. A further complication is that the these two debt exchanges and the Paris Club payment are inter-connected, and the individual success of each may require the successful completion of the other. End Summary.

¶2. (U) This is the second of two cables on the impact of the financial crisis on the GoA's proposed debt deals. Septel discusses speculation that the GoA may delay completion of payment to Paris Club creditors.

Status on Re-opening the Debt Exchange

¶3. (SBU) Although it is getting less press attention than similar concerns about the GoA's ability/willingness to go through with the full payment of Paris Club arrears (septel), the financial crisis is also complicating efforts of a group of foreign banks and the GoA to negotiate a new debt exchange for holders of $19.5 billion face value of untendered debt (see Ref A for background). (These are the so-called "holdout" bondholders, who refused to participate in the 2005 debt exchange stemming from the GoA's December 2001 default).

¶4. (C) This debt exchange proposal is linked to the simultaneous mini-debt swap of Argentine debt coming due 2009-2011 (see Para 10 below), which is similarly constrained by recent events. On October 7, Juan Jose Bruchou (PROTECT), President of Citi-Argentina, which is involved in both deals, told Ambassador Wayne that neither deal is possible in the current market, given that yields on Argentine bonds have leapt from around 17% to 23% since CFK announced September 22 that the GoA would consider entering into these arrangements. (Full conversation with Bruchou reported septel.)

¶5. (C) Cabinet Chief Sergio Massa and the organizing banks (Barclays, Citi, Deutsche Bank) met September 26 to go over the broad outlines of the deals. Based on the positive results of this meeting, Finance Secretary Lorenzino led an Economy Ministry team to New York on October 1 to meet with the GoA's lawyers (Cleary Gottlieb), meet with the U.S. SEC, and begin technical talks with the three banks. Norberto Lopez Isnardi (PROTECT), Director of Public Credit at the Ministry of Economy (reporting to Finance Secretary Hernan Lorenzino), told Econoff October 7 that the visit went well, but reiterated Citi President Bruchou's comment that in the current market there is no deal. However, Lopez pointed out that since negotiations and the documentation process would take two to three months to complete, the two sides will get the two transactions ready to launch as soon as there is a market window.

¶6. (C) Despite the constant press speculation about the details of the Holdout debt exchange, Economy Ministry and Citibank contacts confirm to Post that the two sides have only agreed on broad parameters. However, the key features include an exchange of instruments and the promise of new money. At present, the complication for both of these aspects is that Argentine debt yields, which were already well above emerging markets averages, have spiked in recent weeks in response to the financial crisis. At current yields, therefore, the offers are too expensive for the GoA and unattractive for potential participants.

¶7. (SBU) First, the value of the U.S. dollar-denominated Discount bonds (maturing in 2033) that will be swapped for the untendered bonds have fallen significantly (yields on these Discount 33s have increased to 18.2% as of October 8

from 11.25% in late August). The value of the GDP Warrant that will also be issued in the deal has also fallen (from a high of over $10 per 100 warrants in late August to $6 per 100 warrants on October 8). This makes the deal less attractive to Holdouts. Second, the deal requires participants to pony up new cash, for which they will receive 10-year USD-denominated bonds.

¶8. (C) Since yields on these bonds have jumped recently over 20%, the issuance would either be extremely expensive for the GoA or participants would have to accept a bond with a lower yield, which would immediately drop in value. Either way, it will not work until Argentine debt prices recover significantly. (Norberto Lopez Isnardi told Econoffs that the two sides are analyzing options that include excluding retail investors from the new-cash requirement and -- if market conditions allow -- opening a stand-alone cash tranche.)

¶9. (C) According to Norberto Lopez Isnardi, Finance Secretary Lorenzino believes the GoA will easily convince Congress to approve a new law authorizing the re-opening of the debt exchange. At present, the GoA plans to send a bill to Congress as soon as it reaches agreement with the banks on main guidelines of the exchange and started the legal process (e.g., filing with the SEC, preparing the prospectus).

Mini Exchange Faces Legal and Financial Challenges

¶10. (C) The GoA, Barclays, Citi, and Deutsche Bank are simultaneously negotiating a mini-debt exchange of local debt, with the goal of smoothing the GoA's maturity profile for 2009-2011. (The GoA's financing needs increase by about 50% during this period.) The timeline will be similar to the larger debt swap (completion by year-end). However, since it also has a new money element, both Citi's Bruchou and the Economy Ministry's Norberto Lopez Isnardi say it faces the same challenges as the holdout debt swap and cannot be completed in the current environment.

¶11. (C) This debt swap also faces serious legal hurdles, due to the Holdout lawsuit that succeeded in convincing New York Southern District Court Judge Thomas Griesa to freeze a stock of "Global bonds" backing the Guaranteed Loans that comprise a significant portion of the exchange. GoA lawyers Cleary, Gottlieb hope to meet with Judge Griesa soon to explain the progress of both debt swap transactions, in the hopes that Griesa will change his attitude about Argentina and allow the transactions to go through. (Judge Griesa is reportedly so completely fed up with Argentina that he refuses to allow Cleary Gottlieb lawyers to speak in court.)

Comment

¶12. (C) Another complicating factor is that these two deals and the GoA's plan to pay Paris Club creditors are not mutually exclusive. On the contrary, they are inter-connected and it may be difficult to do any of the three alone. As an explanation, Senior BCRA officials tell Econoff that the announcement of the debt swaps might not have even happened if the GoA had not botched the Paris Club announcement. The GoA's surprise announcement that it would use reserves to pay Paris Club prejudiced the BCRA's legal position in the New York court case with Holdout bondholders over $105 million in frozen BCRA reserves, because it undermined the BCRA's argument that it is an independent body and the reserves do not belong to the GoA (see Ref B for background). Therefore, re-opening the debt exchange will strengthen their position in this and other Holdout lawsuits, since it will show Judge Griesa that the GoA is finally addressing this long outstanding issue. However, for the holdout swap to be successful, it requires a significant improvement in the yields on GoA bonds offered in exchange for tendered holdout debt and guaranteed loans as well as "new money" GoA bonds that are an integral part of the re-financing package under consideration. Ironically, the effects of global turmoil aside, one reason Argentine yields are so high is due to concerns about the GoA's ability to meet its debt obligations during 2009-2011. Therefore, BCRA officials believe that completing the mini-swap and smoothing out the amortization schedule should greatly alleviate this concern and result in reduced debt yields.
WAYNE